

Topic 3: Fiduciary Relationships and Breach of Fiduciary Duty

It is to be advised that [P] may allege that [D] owed a fiduciary duty to them and [D] breached fiduciary obligations by [conduct]. Fiduciary duties are underpinned by a relationship where one party is in a position of vulnerability and reliant on the other (Hospital Products). The protective purpose is to safeguard one's interest in exacting undivided loyalty by requiring the fiduciary to entirely subordinate their interests to those of the principal and is thereby prevented from engaging in self-promoting conduct.

- Vertical non-associative relationships refers to when fiduciary duties are owed on a one-way basis whereas horizontal associative relationships refers to when fiduciary duties are owed on a multilateral basis (eg partners).

Element 1: Is there a fiduciary relationship (FR)?

In order to attract equity's protection, the relationship between [P] and [D] must be fiduciary, which must be established either through a settled category, or established in fact (Hospital Products).

Settled Category?

Historically, courts have recognised some relationships as being categorically fiduciary in nature. If so, equity recognises that a FR arises as a matter of legal inference and P is not put to proof on the matter.

- *No Settled Category*: OTF, the relationship between [D] and [P] does not fall within an accepted category.

OR

- *Settled Category*: OTF, the relationship between [P] and [D] is one of [accepted category] and therefore equity will take it as a given that [D] stands in a fiduciary capacity vis a vis [P].

Trustees to beneficiaries (Keech)

If [D] holds property on trust for [P], [D] and [P] will be regarded as being in a trustee-beneficiary relationship which is the paradigmatic fiduciary relationship (Keech). This is because [D] as trustee and legal owner of the property is in a considerable position of power vis a vis [P] as beneficiary who has beneficial/equitable ownership of the trust property.

Directors to companies (Regal)

Since [D] is a director of a company, namely [company] and a fiduciary relationship is deemed to exist between a director and company, the court would take it as a given that [D] stands in a fiduciary capacity vis a vis [company] (Regal). [D] categorically owes FD to [P/company].

Equity recognises the existence of a fiduciary relationship in this circumstance since companies, whilst a separate legal entity from directors and shareholders, are unable to make decisions independently of directors and thus depend on directors and are in a vulnerable position since directors may abuse their powers.

Agents to principals (McKenzie)

The court may find that [D] is [P]'s agent since [D] is in a representative capacity acting on [P]'s behalf in doing [X]. Since equity has recognised the agent-principal relationship as inherently fiduciary (McKenzie; Boardman), [D] would be deemed to stand in a fiduciary capacity vis a vis [P].

- Real estate agent is an agent for the vendor. In McKenzie, D was a real estate agent that lied to her about what price she would get for her farm so that she could buy it for cheaper herself.

Employees to employers (Warman)

Since [D] is employed by [P] and the court has recognised that employer-employee relationships are inherently fiduciary (Reid), the relationship between the parties would be deemed to be fiduciary in nature because employers are vulnerable to the decisions and conduct of their employees.

- May need to be a senior employee, or an employee who has the ability to impact the interests of the employer – there is conflicting dicta from intermediate appellate courts on this point. Lower-level employees have limited ability to influence, and a limited scope.
- In *Warman*, Dwyer was the general manager of the Queensland branch of the company and was a fiduciary due to his seniority and ability to engage clients.

Partners (Chan)

Since [P] and [D] are co-partners together forming a partnership which is a relationship that equity has recognised as inherently fiduciary (Chan), [D] stands in a fiduciary capacity vis a vis [P] and vice versa. Equity recognises partners as owing fiduciary duties to one another since parties share assets and opportunities on a basis of mutual confidence – skill and information brought by parties to the relationship in the pursuit or achievement of a common financial goal (UDC). This is an example of a horizontal fiduciary relationship since parties owe fiduciary duties to one another that is neither party occupies a dominant/more powerful position vis a vis the other.

Joint ventures

Joint venturers may owe fiduciary duties to one another if the joint venture takes the form of a partnership (UDC) – apply test from *Dawson J* below.

Whether a joint venture is fiduciary depends on the form it takes:

- Carrying on business in partnership with a common view of profit.
- The mutual confidence between the parties creates the fiduciary relationship.

Solicitors to clients (Nocton)

Since [D] and [P] are in a solicitor–client relationship which equity recognises as inherently fiduciary (Nocton), [D] would stand in a fiduciary capacity vis a vis [P]. The basis of this implied relationship is that a solicitor has expert knowledge and undertakes to act on their client's behalf.

Bankruptcy trustees to creditors

Not accepted categories:

- Guardian and Child (may be under specific circumstances)
- Parent to child
- State to children
- Doctor to patient (Breen)** → (in some cases, there will be a fiduciary relationship)
- Giving of advice doesn't give rise to fiduciary relations (Pilmer; Breen)

Though the facts likely give rise to an accepted category of fiduciary relationship. However, in the event that this conclusion is wrong, I will also go through a factual fiduciary relationship analysis.

Factual FR?

Despite the relationship between P and D is likely not an accepted fiduciary relationship, the categories are not closed and a non-standard FR may exist as a matter of fact (*Hospital Products*).

- *Horizontal Associative Fiduciary Relationships (eg joint ventures*)*: Relevantly, the existence of an horizontal associative fiduciary relationship may be established in fact per the mutuality of confidence and trust test in UDC. If P can establish that the parties came into the association based on the same mutual trust and confidence and requiring the same good faith and fairness as if a formal partnership deed has been executed, then they will each owe fiduciary duties to one another (UDC). **Akin to UDC owing fiduciary duties**, P would argue that though the relationship with D was not formally characterised as a partnership, equity is not concerned with the form or label of an association but its substance meaning (UDC).
- *Vertical Non-Associative Relationship*: Relevantly, the existence of a non-associative FR may be established here in fact per the 3-point undertaking test articulated by Mason J (*Hospital Products*).

- *Undertaking*: Firstly, the putative fiduciary [D] must have made an undertaking to act on behalf of the alleged principal [P] in a representative capacity with respect to a particular function or responsibility, which is satisfied here because D agreed to [manage property for the beneficiary's benefit or manage a corporation's affairs on behalf of the corporation].
- *Entrusting*: Secondly, the function or responsibility must have been entrusted to the putative fiduciary D with the power and discretion to affect the principal's legal or practical interests, which is satisfied here because [throughout the contract terms and practical course of the relationship, D could...].
- *Vulnerability*: Thirdly, in exercising this function or responsibility the putative fiduciary must have had a special opportunity to act to the detriment of the principal rendering the latter vulnerable to the fiduciary's abuse, which is satisfied here because [of P's inexperience and D's autonomy and independence from P's supervision].

Considerations:

- *Commercial arm's length transaction*: [fiduciary] would argue that the relationship can be characterised as a commercial contractual relationship where each party engaged one another on an equal footing and at arm's length with a view to each other's self-interest. Therefore, [fiduciary] would argue the relationship here is unlikely fiduciary in nature given the commercial context and the fact that D is not required to subordinate their self-interest and not required to act exclusively in the interests of P (Hospital Products) akin to how **the commerciality of a transaction and the underlying profit-motive of both HP and USSC presented a significant obstacle to the finding of a FR in Hospital Products**.
- *Contractual Relationship*: Given a contract may often provide the foundation of a FR, [principal] would submit that equity may supplement contractual terms with fiduciary duties provided they accommodate to contractual terms so they are consistent with and conform to them (Hospital Products). [principal] would argue that – **unlike in Hospital Products where it was found that a comprehensive FR was inconsistent with the distributorship contract because it allowed HP to comply with the best-efforts clause whilst advancing own interests** – fiduciary duties here would be compatible with the contract and that there therefore could be a FR. However, [fiduciary] would argue that the finding of a FR would alter the operation which the contract was intended to have and therefore cannot accommodate fiduciary duties – **akin to how a finding of FR between HP and USSC would alter the best-efforts clause in Hospital Products**.
- *Doctor-Patient Relationship*: P would argue that [doctor] owed [patient] fiduciary duties because they were in a doctor-patient relationship. However, D would counterargue that a doctor-patient relationship – which is primarily a contractual relationship – has been found not to be a FR given that doctors do not act in a representative capacity for their patients (but simply in the exercise of their professional responsibilities) and equity is reluctant to impose such onerous duties on someone who has not voluntarily assumed them – **akin to how Dr Williams was found not to owe fiduciary duties to Breen in relation to accessing her medical records** (Breen). Indeed, Gummow J remarked that even assuming the doctor-patient relationship to be a FR, the scope of such a relationship would be confined to the provision of medical treatment (excluding the right to access medical records) (Breen).
- *Provision of Advice*: Merely providing advice would not constitute acting on behalf of/ representative character nor would mere reliance since this is characteristic of many relationships even those which are not fiduciary in character (Breen).
- *Rejection on other grounds*: A relationship bearing fiduciary characteristics still may be rejected by the court on other grounds (Habib) **akin to how the court refused to recognise a FR between the Commonwealth and a citizen based on policy concerns**.

Therefore, because P and D have a FR, D owes P fiduciary duties.

Element 2: Scope of Fiduciary Relationship

It must be ascertained whether D's impugned misconduct of [diverting a lucrative client contract] falls within the scope of the FR and the subject matter over which the fiduciary obligations/duties extend (Birtchnell). This is a question of fact having regard to the functions and responsibilities the fiduciary has undertaken to the principal (Grimaldi).

- The scope of the FD can be both ascertained from the nature of the agreement or contract governing the relationship like the distributorship contract in (Hospital Products) or the actual course of dealings (Birtchnell) with the latter being especially relevant when the reality of the relationship is different from the contract. In Birtchnell, though the partnership agreement only spoke about facilitating clients with the sale of property (not development), it was held that the partnership went beyond the deed and that in reality they were helping clients to buy and then developing too.
- The scope of an agency relationship is generally circumscribed and narrow insofar that agents are appointed for specific purposes/tasks where the relationship ceases after completion (Grimaldi).
- The scope of a company director is generally broad (Grimaldi).
- Partnership relationships often evolve over time and the scope can expand or contract (Grimaldi).

Here, having regard to the [nature of the agreement like the distributorship contract in Hospital Products/actual course of dealings like in Birtchnell], the scope of the FR would likely entail D's function/responsibility of [include]. Accordingly, D's misconduct [thematically/temporally] likely falls within this scope.

Element 3: Breach of Duty

In order to avoid disloyal conduct, fiduciaries must not enter into transactions that breach either the profits or conflicts rule (Chan). [D]'s act of [act] may be a BOFD as it amounts to an unauthorised profit/conflict. As breach is determined objectively, subjective intention is irrelevant (Boardman) and detriment is not necessary for a breach (Keech).

- *Prospectivity: Equity imposes proscriptive fiduciary obligations (Breen) - if you are saying they have breached fiduciary duties because they have failed to do a positive act, then rethink.*
- *Subjective Honesty Irrelevant:* D may argue that they [did not think themselves as acting disloyally but rather was motivated by good intentions]. However, P would submit that given equitable liability is strict here, the subjective honesty of the fiduciary is immaterial and it does not matter whether the fiduciary didn't think themselves as acting disloyally (Keech; Boardman) – akin to how Sandford was held to be in breach of fiduciary duties despite his bona fide honest attempts to renew the leasehold estate on trust (Keech) OR akin to how Boardman and Phibbs were held to be in breach of fiduciary duties despite their honest endeavours to protect trust property by acquiring the additional shares in Lester & Harris Ltd which ended up financially assisting the trust (Boardman). Accordingly, the subjective intentions of the fiduciary is irrelevant in respect of the imposition of fiduciary liability.
- *P's Inability to Pursue Opportunity:* D may argue that there was no disloyalty because P was unable or unwilling to pursue the opportunity anyway. However, P would counterargue that the fact that the principal was unable or unwilling to pursue the profitable opportunity the fiduciary exploited does not therefore legitimise the fiduciary's exploitation of the opportunity (Keech; Boardman) – akin to how Sandford was still disqualified from renewing the leasehold estate for his

own benefit despite Keech being unable to renew the lease on trust (Keech) OR akin to how Boardman and Phibbs were still disqualified from acquiring the additional shares in Lester & Harris Ltd by virtue of their fiduciary position as agents of the trust (Boardman).

Conflicts rule

Interest-duty conflict:

- *Possibility of Conflict:* Relevantly, P would submit that the fiduciary has breached the conflicts rule here because D has failed to avoid a position where their self-interest and duty of undivided loyalty to P possibly may conflict insofar that [reason] (Boardman) (i.e. interest-duty conflict). P would argue that there is more than a mere theoretical possibility of conflict but rather a real, sensible possibility of conflict (Boardman; Chan) because [reason] – akin to how Mr Boardman and Tom Phibbs as agents breached the conflicts rule by acquiring additional shares in Lester & Harris Ltd which the trustees may have wanted to acquire (Boardman).
- *Actual Conflict:* Relevantly, P would submit the fiduciary has breached the conflicts rule here because that there has been an actual conflict between D's self-interest and their duty of undivided loyalty to P (i.e. interest-duty conflict) insofar that [reason] – akin to how solicitor Mr Nocton actually breached the conflicts rule by providing self-advancing advice to Lord Ashburton in relation to a mortgage transaction that created a conflict between Nocton's personal economic interest in seeing his business partner Mr Baring succeed financially and his duty of undivided duty of loyalty to Ashburton (Nocton).

Duty-duty conflict: Relevantly, the fiduciary may have breached the conflicts rule here because they failed to avoid a position where their concurrent duties of loyalty to multiple principals may conflict (i.e. duty-duty conflict) insofar that [D has acted to further the interests of one principal potentially to the prejudice of the other] – akin to how Rowe, McBride & Partners breached the conflicts rule by advising Farrington to invest in a property development group that also happened to be a client of the firm; creating a conflict the firm has in relation to their concurrent duties of loyalty to both clients (Farrington).

Survivability of Fiduciary Duties Despite Cessation of FR

Fiduciary relationship Completed: P would submit that D had engaged with [individual directors] in the past and there was therefore a conflict between their duty to [the individual directors] and the [company]. However, D would argue that the fiduciary engagement or relationship with [third party] was completed and there was therefore no concurrent duties – akin to how Mr Pilmer's duty to the individual directors of Duke Group in the past had been completed and therefore there is no possible conflict between Duke Group and its individual directors (Pilmer).

- However, P would submit that fiduciary duties can outlive or persist beyond the duration of a FR in some circumstances –
- Akin to how Dr Chan continued to owe Dr Zacharia fiduciary duties for the purpose of winding up the partnership and therefore acted disloyally in renewing the lease despite the cessation of the FR (Chan).
- Akin to how Mr Schmidt continued to owe AHR Kalimpa Pty Ltd fiduciary duties as a former director and was disqualified from pursuing a particular opportunity post-resignation because he pursued it during his time as director and was not a 'fresh' opportunity (Schmidt).
- Akin to how it was found that solicitors can continue to owe fiduciary duties to their former clients and could potentially be inhibited from acting against former clients if the solicitor is acting for another client in relation to the same matter (Spincode Pty Ltd).

Profits Rule

Relevantly, the fiduciary may have breached the profits rule insofar that they obtained an unauthorised benefit/gain in the form of [profit] by reason of their fiduciary position without the consent of the principal.

- Here, P would submit that D obtained a material gain from diverting an opportunity from the principal (Chan) – **akin to how Dr Chan diverted the profitable opportunity of renewing the leasehold estate for 2 further years away from the partnership and Dr Zacharia (Chan).**
- Here, P would submit that D as co-joint venturer acquired a benefit not disclosed to any other collaborating party (UDC) – **akin to how UDC obtained a security interest without Brian's knowledge (UDC).**
- Here, P would submit that D acquired a benefit/gain from exploiting knowledge or opportunity obtained in their fiduciary capacity – **akin to how the 4 directors of Regal Ltd used the information they obtained by virtue of their office of directors to profit from a transaction (Regal) OR akin to how Boardman and Phibbs acquired the additional shareholding as a result of position as agents (Boardman).**
- Here, P would submit that D as fiduciary accepted bribes/secret commission – **akin to how Mr Reid accepted bribes to obstruct the prosecution of high-profile criminals and thus violated his fiduciary duty of loyalty to his employer (Attorney General for Hong Kong).**

Accordingly, it prima facie appears D has breached their fiduciary duties in relation to P by breaching the conflicts/profits rule.

Defences

D's breach of fiduciary duties may be excused if they acted with the full knowledge and consent of the principal (Regal). This requires the errant fiduciary's prior full and frank disclosure of all material facts and the principal to consent to it, which is a high threshold.

- **In Boardman, the defence failed because Boardman and Phibbs only sought the fully informed consent of Mr Fox; not the other trustees and beneficiaries.**
- In director-company contexts, the consent is given by shareholders (Queensland Mines).

Third Party Liability (Can only get personal remedies)

Where there has been a breach of fiduciary duties, P may sue a third-party stranger such as [third party] who is extraneous to the fiduciary relationship that has participated in the fiduciary's wrongdoings under the separate causes of action of knowing receipt and knowing assistance (Barnes). Both causes of actions are parasitic upon P's prior proof of the fiduciary's breach of duty.

Knowing Assistance (Second Limb)

Personal liability is imposed on third parties who knowingly assist a fiduciary's dishonest and fraudulent breach. P must prove the 3 elements.

- *Seriousness of Fiduciary's Wrongdoing Requirement*

Firstly, the fiduciary must have pursued a dishonest and fraudulent design (Farah Constructions), which is conduct which itself is 'unconscionable' and transgresses 'ordinary standards of honest behaviour' (Hasler; Lifeplan). **Akin to in Consul Development where Mr Grey of DPC Estates dishonestly diverted a profitable opportunity from the company for personal gain**, P would argue this element is satisfied because [reason].

- This is an objective standard uninterested in subjective dishonesty or otherwise. What would the reasonable person think about the fiduciary's conduct?
- *Assistance Requirement*

Secondly, the third party must have assisted with the 'execution' of fiduciary's dishonest and fraudulent breach (Lifeplan). Mere passive acquiescence is not sufficient to establish assistance because the knowing assistant must 'forward or advance the primary breach' (Ferguson). OTF, **akin how Consul Developments actively assisted the fiduciary in their breach by acquiring the**

properties and therefore advanced Mr Grey's dishonest and fraudulent design (Consul Development), P would likely make out this element insofar that [the third party has actively assisted...].

- *Knowledge Requirement*

Thirdly, P must demonstrate that the third party had the requisite level of knowledge of the fiduciary's breach, which is satisfied by knowledge from level 1-4 on the Baden Scale (Farah Constructions). Here, P would argue that – **unlike in Consul Development where Clowes did not have the requisite level of knowledge of Mr Grey's dishonest breach insofar that he was told that DPC Estates was not in the market for the properties due to financial reasons** –

Actual knowledge

- The third party had a clear and direct knowledge of the fact indicating the dishonesty, which supports an inference of actual knowledge (ie category 1). This is because [reason].
- The third party wilfully shut their eyes to the obvious, which supports an inference of actual knowledge (ie category 2). This is because [reason].
- The third party's suspicion was aroused but wilfully and recklessly failed to make such inquiries as an honest and reasonable man would make amounting to 'calculated abstention' (Grimaldi), which supports an inference of actual knowledge (ie category 3). This is because [reason].

Constructive knowledge

Categories 4 and 5 support inferences of constructive knowledge rather than actual knowledge.

- The third party had knowledge of circumstances which would indicate the fact of the fiduciary's dishonesty to an honest and reasonable man rendering them 'morally obtuse', which supports an inference of constructive knowledge (Farah) (i.e. category 4). This is because [reason].
- The third party had knowledge of circumstances which would put an honest and reasonable man on inquiry, which is insufficient. Australian courts are unwilling to extend sufficiency to category 5 knowledge as there is no wilful failure to make enquiries, merely negligence (i.e. category 5). This is because [reason].

Therefore, the second limb of *Barns v Addy* is likely made out as [third party] has knowingly assisted [fiduciary] in their dishonest and fraudulent breach of their fiduciary duties to [principal].

Knowing Receipt (First Limb)

A third party will be personally liable if P can prove they beneficially received fiduciary property with the knowledge the property was transferred to them in breach of fiduciary duty. P must satisfy 2 elements.

- *Beneficial Transfer of Fiduciary Property*

Firstly, the property transferred to the third party must be property held or controlled subject to a fiduciary obligation (Grimaldi). Here, P would satisfy that the property is fiduciary property because [it was held within the relevant fiduciary relationship and to which fiduciary duties attached].

- Information giving rise to a profitable opportunity is not property for *Barnes v Addy* purposes – **akin to how the information concerning the value of acquiring the 2 adjoining properties was not held to be property** (Farah).
- This extends to corporate property (Grimaldi).

In addition, the fiduciary property must be received beneficially in the sense of it being in the third party's name and for their benefit and must be 'doing more than acting as a mere depository or channel' (Quince). Here, this is satisfied because [reason].

- *Knowledge*

P must demonstrate that the third party knew they received property in breach of fiduciary duty, which is satisfied by knowledge from level 1-4 on the Baden Scale (Farah Constructions). Here, P would argue that:

Actual knowledge

- The third party had a clear and direct knowledge of the fact indicating the fiduciary's breach, which supports an inference of actual knowledge (ie category 1). This is because [reason].
- The third party wilfully shut their eyes to the obvious, which supports an inference of actual knowledge (ie category 2). This is because [reason].
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Remedies for Barnes v Addy

Liability under Barnes v Addy can only make [third party] personally liable to P (Grimaldi). Where there are multiple equitable wrongdoers such as a fiduciary and third party, P can seek different equitable remedies against them and may receive a different measure of remedy (Nicholls; King Network Group).

- *Knowing Assistant*: Where a knowing assistant has made their own profits separate to those made by the fiduciary, these too can be disgorged via an account of profits (Lifeplan) – **akin to how Lifeplan not only sought an account of profits from the errant fiduciaries Mr Woff and Corby but also knowing assistant Foresters**. Go to Account of Profits analysis.
- *Knowing Receipt*: where a knowing recipient receives property, the remedy typically sought is equitable compensation assessed at the value of the fiduciary property. Go to equitable compensation analysis.

Proprietary relief: However, P can still seek proprietary relief against [third party] as a third party outside the Barnes v Addy framework in order to vindicate P's prior/superior equitable interest in [profits/capital gains] by conducting a tracing exercise (Foskett). Go to tracing into third party analysis.